GLOBAL FEDERATION OF INSURANCE ASSOCIATIONS

To: Tara-Lea Herkert
Reinsurance Review Committee
Office of the Superintendent of Financial Institutions
255 Albert Street
Ottawa, Ontario
Canada

Cc: Judy Cameron, Senior Director
Neville Henderson, Assistant Superintendent Insurance Supervision Sector
Ben Gully, Assistant Superintendent Risk Support Sector

Date: 3 September 2019

Subject: Global Federation of Insurance Associations comments on OSFI draft revised guideline B3

Dear Ms Herkert,

The international insurance industry, as represented by the Global Federation of Insurance Associations (GFIA) is concerned with the proposed changes associated with OSFI's Reinsurance Framework, as outlined in OSFI Discussion Paper issued in June 2018. GFIA provided its initial views on OSFI's Discussion Paper in a letter dated 2 July 2019.

To reiterate, GFIA takes the view that the proposals, and in particular the policy limit rule, would have a detrimental effect on global commercial insurers operating in Canada and their policyholders. Under the proposed rule, OSFI is asking P&C insurers to be fully capitalised against the three extremely remote loss scenarios. P&C insurers in Canada have tested the outcome of the proposed rule, and concluded that, if implemented, OSFI would require an additional $21 to $30 billion CAD in excess capital raised by large commercial writers or excess collateral from global reinsurers to bridge the gap. The stress scenarios are far too extreme and the capital gap is too large to be afforded by these companies. GFIA advises against introducing such extreme policy measures, as they are not consistent with how insurance companies are regulated around the world. GFIA is of the view that that the ultimate outcome would be a shortage of capacity for specialised types of risks and industries (e.g. aviation, nuclear, oil and gas, large construction projects, etc.). GFIA would be pleased to provide further comments and insights when OSFI's draft Guideline B2 is released for comment.

In this letter, GFIA is writing to comment on the draft revisions to Guideline B-3: Sound Reinsurance Practices and Procedures, released on June 12, 2019. GFIA finds the following statement on page 3 of the draft Guideline of particular interest as it appears to be out of line with how insurance regulators around the world perceive transfer of insurance risk:

"…OSFI will generally not recognise or grant credit for a foreign FRI's reinsurance arrangement(s) when risks insured in Canada are ceded back to the foreign FRI's home office through affiliated reinsurers"

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Withholding capital credit for foreign reinsurance arrangements through affiliate transactions that transfer insurance risk to the home office will discourage global commercial insurers from participating in the Canadian market. Intra-group reinsurance arrangements are a legitimate and effective risk management tool that underpins global management of risks, covers extreme losses and increases insurers' underwriting capacity. It is a model that has proven to work for decades in jurisdictions around the world. Reinsurance arrangements in foreign jurisdictions are regulated by the respective regulatory authorities that operate under similar mandates as OSFI to protect domiciled insurers and their policyholders. The quality of those regulations should be taken into consideration by OSFI. This premise is stipulated by the International Association of Insurance Supervisors (IAIS) under Insurance Core Principle (ICP) 13.4 (When supervising ceding insurers purchasing reinsurance across borders, the supervisor takes into account the supervision performed in the jurisdiction of the reinsurer)[1].

Given the above, GFIA notes that foreign federally regulated insurers' (FRI) home offices typically have a significant capital base to cover extreme losses should they occur in multiple jurisdictions simultaneously. In the event of a distress situation in Canada, a reinsurance arrangement between the foreign FRI insurer and their home office includes a legal, contractually binding obligation by the home office to cover the loss.

As such, GFIA recommends that OSFI consider cooperating with supervisory authorities in jurisdictions where foreign (re)insurance groups are headquartered in order for OSFI to have enhanced oversight of the counterparty risks related to cross-border reinsurance of foreign FRIs. The OECD's December 2018 research paper titled "The Contribution of Reinsurance Markets to Managing Catastrophic Risk" also encourages regulatory cooperation, as evident in the following statement:

"…ensuring that reinsurers are appropriately supervised in their home jurisdiction and enhancing supervisory cooperation and information exchange across jurisdictions, might offer a better means to ensuring that counterparty and execution risks related to cross-border reinsurance are properly managed while reflecting the global nature of reinsurance markets" (p. 7)[2].

Lastly, OSFI's proposals are generally inconsistent with the approach taken by the EU Solvency II regulation, the US RBC regulation, the EU-US Covered Agreement, Bermudian and Australian regulations, as well as the United States-Mexico-Canada Agreement (USMCA) signed on November 30, 2018. The USMCA preserves key elements of the previous North America Free Trade Agreement (NAFTA), including the treatment of cross-border financial services. Market access principles prohibit host nations from imposing certain quantitative restrictions that would limit the export of financial services to the host country. Consequently, insurance regulators within each jurisdiction could not discriminate against foreign-based (re)insurers by imposing different solvency, capital requirements or market conduct standards required of domestic (re)insurers.

[1] https://www.iaisweb.org/page/supervisory-material/insurance-core-principles//file/77903/all-adopted-icps-updated-november-2017
[2] https://www.oecd.org/finance/the-contribution-of-reinsurance-markets-to-managing-catastrophe-risk.pdf

Given the views of the IAIS and OECD and above-mentioned regulatory matters, GFIA encourages OSFI to reconsider the proposed regulatory framework, including the proposed revision to Guideline B-3.

GFIA would gladly welcome further discussions with OSFI on these and related matters.

Kind regards,

Brad Smith
Chair of the GFIA Trade working group (BradSmith@acli.com)

About GFIA

Through its 41 member associations and 1 observer association, the Global Federation of Insurance Associations (GFIA) represents the interests of insurers and reinsurers in 64 countries. These companies account for around 89% of total insurance premiums worldwide. GFIA is incorporated in Switzerland and its secretariat is based in Brussels.